

ARGO ASSOCIATES

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The Philippines – Midterm Elections boost for Duterte

The Philippines held its midterm elections on 13 May, with over 18,000 positions up for election; the most crucial vote was for 12 seats within the 24-member Senate. The new senators, who will serve till 2025, constitute nine candidates allied with incumbent President Rodrigo Duterte and three independents, with no candidates from the opposition. The changes will leave only four members of the opposition – one of whom is being detained on alleged drug charges – in the entire Senate (which has thus far resisted some of Duterte's most extreme policies). This is a resounding endorsement for Duterte and his policies and comes after a recent approval rating of 81% in May for his administration, according to the reliable local pollster Social Weather Stations.

'Aye' for Dutertes, 'nay' for opposition, some political dynasties lose out

Duterte's popularity in this election was so evident that two new senatorial candidates he endorsed – former aide Christopher Lawrence "Bong" Go and former Philippine National Police (PNP) chief Ronald "Bato" Dela Rosa (known as the face of Duterte's war on drugs) – won the Senate polls in third and fifth place respectively. This happened despite their lack of national prominence before Duterte's ascent to power. Bong is expected to play the role of intermediary between the Senate and the Malacañang Palace to ensure the smooth implementation of Duterte's legislative agenda. Meanwhile, Bato's task will likely be to support Duterte's war on drugs, evident in his request to be chair of the Senate committee on public order and dangerous drugs, which conducted an investigation into the war on drugs when he was PNP chief.

As well as Duterte's triumph in the Senate, all three Duterte children secured strong victories in their political bids in the stronghold of Davao. Daughter Sara and youngest son Sebastian won the Davao mayor and vice-mayorship, while oldest son Paolo secured the first legislative district seat and is currently eyeing the post of House Speaker. Sara is also considered to be a strong potential candidate for the 2022 presidential race.

The opposition's crushing defeat was partly due to the lack of a cohesive campaign, apart from criticism of Duterte's unorthodox leadership and the administration's economic policies, weakened by inflation-detering measures implemented prior to the midterms. It is surprising that even prominent opposition candidates placed slightly outside the 12 senatorial seats. Those high-profile figures include Manuel 'Mar' Roxas III, former Interior Secretary and 2016 presidential candidate, and Paolo Benigno 'Bam' Aquino IV, cousin of former president Benigno 'Noynoy' Aquino (2010-16).

Another notable development in this election was the lacklustre performance of the prominent Estrada and Binay political dynasties, helmed respectively by former President Joseph 'Erap' Estrada and former vice-president Jejomar Binay. The Estradas lost almost every single post contested, while the Binays also sustained several blows, with family patriarch Jejomar losing his congressional bid in economically important Makati City, where he built his political dynasty. Both

families have faced allegations of corruption but, despite their lack of success in these elections, they retain major business and political networks across these regions and will likely remain politically active - they could even stage a comeback in the next elections.

Push for federalism and tax reform

Duterte's current hold over the Senate gives him greater power to pursue his policies, some of which have been delayed because of infighting between the House of Representatives (HOR) and the Senate. For instance, the 2019 budget was only approved this April after months of delay, causing a delayed injection of funding for state-funded projects and the lowest first-quarter economic growth in four years (at 5.6%). Duterte's policy priorities include a plan to cut corporate taxes, federalise the government, remove presidential limits, and reinstate the death penalty.

A bill promoting federalism – which includes options for provinces to be recognised as federal states and removes current limits for senator, district and party-list appointments – has already passed its final reading in the HOR but faced opposition in the pre-midterm Senate. The bill – which has a growing likelihood of passing in the new Senate – will likely have to re-navigate the HOR and Senate when the 18th Congress opens on 22 July. Federalism is likely to be a negative development for investors, as it will increase bureaucracy and the risk of corruption by raising the number of regulations and stakeholders involved from both national and provincial levels. It might also firm up the control of political dynasties over various regions, exacerbating corruption and inequality. To be fair, if it is implemented with the objective of good governance, growth opportunities in decentralised regions could potentially increase; unfortunately, though, given the prevalence of corruption and the weak culture of governance, federalism is more likely to exacerbate corruption risks than boost development in decentralized regions.

The plan to gradually cut corporate tax rates (from the current 30% to 20%) and modernise an antiquated tax collection system comes under the TRAIN 2 or TRABAHO bill. While the bill will be positive for foreign investors overall, it also involves the proposed removal of tax incentives such as the 5% tax on gross income paid in lieu of all local and national taxes, currently offered by investment agencies such as the Philippine Economic Zone Authority (Peza), which will be detrimental to investors in economic or industrial zones.

Other amendments which will be positive for investors and are likely to be expedited under the new senatorial slate include the proposed amendment to the Foreign Investments Act of 1991, lifting restrictions on professions that foreigners can participate in, and encouraging more foreign investment in the small and medium enterprises (SME) sector. A proposed amendment to the Public Investments Act will limit the definition of “public utilities” to electricity and water services, eventually allowing foreign investors to fully own a telecommunications venture. This should also boost the Philippines' weak telecommunications infrastructure.

Challenges remain

Despite support for Duterte's policies, his persistently unpredictable decision-making style means the risk of regulatory uncertainty will remain. For instance, in April, Duterte called for a review of all government contracts, raising concerns about the stability of contracts previously signed with the government. The Department of Justice has said a report on the review will be released around the end of May, focusing on foreign loan contracts with China and water concession agreements, and it seems unlikely that the review will extend to cover all contracts.

Duterte also remains controversial internationally for his war on drugs and support for measures such as the death penalty, meaning the security risks linked to the drug war will persist. The domestic security environment will generally remain a business operational risk in a country afflicted by active militancy, with several militant groups possessing the capability to launch attacks in parts of the Philippines; the Bangsamoro Organic Law (BOL) will also not eliminate the intense security risks in Mindanao any time soon. Furthermore, there are concerns among the Filipino elite regarding Duterte's foreign policy, particularly the relationship with China given the latter's increasing activity in the South China Sea. Lastly, observers will closely watch the 74-year-old's health - with reports of Duterte missing key meetings during international conferences and his non-appearance in public for a week after the midterm elections - given the uncertainties about how his potential departure from the politics would impact wider political stability.

Politicking for 2022 begins

Moreover, not all the nine pro-Duterte senators will necessarily continue to support him once the new session of Congress begins. Some senators might have pledged loyalty to Duterte to ride on his popularity but may then begin to push their own agenda in the coming months. Crucially, a split of alliances will likely begin in the coming months as various parties prepare their 2022 bids, pitting them against Duterte and his family.

The Dutertes' success in these midterms provides a platform for Sara to launch her highly anticipated presidential bid in 2022, which she has said she will decide on by January 2021. Duterte will likely lobby for Sara or Bong to succeed him. Former Philippine presidents have faced incarceration and the threat of criminal investigations after leaving office, and Duterte will be no exception, especially given his controversial drug war.

However, other individuals currently allied with the Duterte family might consider a 2022 bid. Ferdinand 'Bongbong' Marcos Jr, who failed in his 2016 vice-presidential bid, might launch a presidential bid. The family appears to be making a comeback, given sister Imee Marcos' recent winning bid for a Senate seat. Bato also hinted in 2017, when he was still PNP chief, that he might consider a presidential bid. Other potential contestants include Cynthia Villar, whose family has provided significant financial support to Duterte.

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About Argo Associates

We seek to provide our clients with the information and intelligence that will allow them to navigate acquisitions, investments, disputes, or frauds in a clear-sighted and rational way, minimizing risk and maximizing opportunities.

Information gathered may clarify the profile and background of key business people and managers; it could illuminate the operations of a company or demonstrate a history of fraud or mismanagement; or it could help our clients to assess the political situation in a given jurisdiction and how it may affect their investments or business operations.

Headquartered in Hong Kong, Argo Associates assists clients across Asia and – through international partners – globally.

Intelligence Gathering

“Intelligence” is central to making sense of the world and to decision-making. Argo Associates has developed a network of well-placed human sources across Asia and – through our partners outside Asia – globally. This network provides insights beyond what is available publicly – into leadership, operations, strategy, corruption, red flags, political connections and so on - and is supplemented by extensive research and analysis of publicly available sources – corporate filings, litigation filings, regulatory communications, media articles, social media postings and so on. In a world in which information is increasingly commoditized, high-level intelligence and analysis provides the insights that give our clients an edge over their competitors.

Fraud, Corruption and Disputes

Our intelligence-gathering techniques and in-depth research and analysis have also helped our clients uncover frauds within their operations or in those of a portfolio company or recent acquisition. Our professionals have provided numerous reports for arbitration or legal proceedings to recover the proceeds of fraud. We have also assisted clients in tracing assets globally when bringing a high-value claim against a company or individual. In high-profile disputes we have assisted top law firms in gathering information, evidence and intelligence in support of their clients’ cases.

Political Risk

Our political risk work has developed naturally out of our intelligence and investigative capabilities. We see political risk as an important part of the evaluation of many investments, mergers and acquisitions, as well as a key element of commercial disputes in many markets. We have helped our clients look at political risk in a new way, not just in terms of the broad outline of potential political developments in various countries, but with a focus on the impact on their businesses. For example, will growing frictions between two countries lead to tariffs that could impact the specific sector in which a portfolio company operates? Or, how will rising protectionism in a country alter the possibility of a fair result in an ongoing commercial dispute? Frequently, politics is local as much as national and we understand the importance of drilling beneath the widely-circulated opinions to a real understanding of what is happening.



Jason Wright, Managing Director of Argo Associates

Prior to founding Argo, Jason was a Managing Director in Hong Kong for Kroll. Before moving to Asia in 2011 he worked for Kroll in Italy for five years and then briefly in London.

In addition to assisting clients on numerous transactions, investigations and disputes in Asia and Europe, - particularly private equity funds, banks, hedge funds and special situations investors - Jason has also specialized in the analysis of political risk, whether that has involved examining the role of local politicians, regulators and other stakeholders, or broader geopolitical concerns.

Although he has managed projects across the whole Asia-Pacific region he has been particularly focused on China, Korea, and Southeast Asia, especially Indonesia, Vietnam, Malaysia and Thailand.

Jason is a scholar of St. Catherine's College, Oxford, having been awarded a Master of Arts (Oxon) in English Language and Literature, as well as a Master in State Management and Humanitarian Studies from La Sapienza University in Rome, Italy.

Lina Gautama, Director

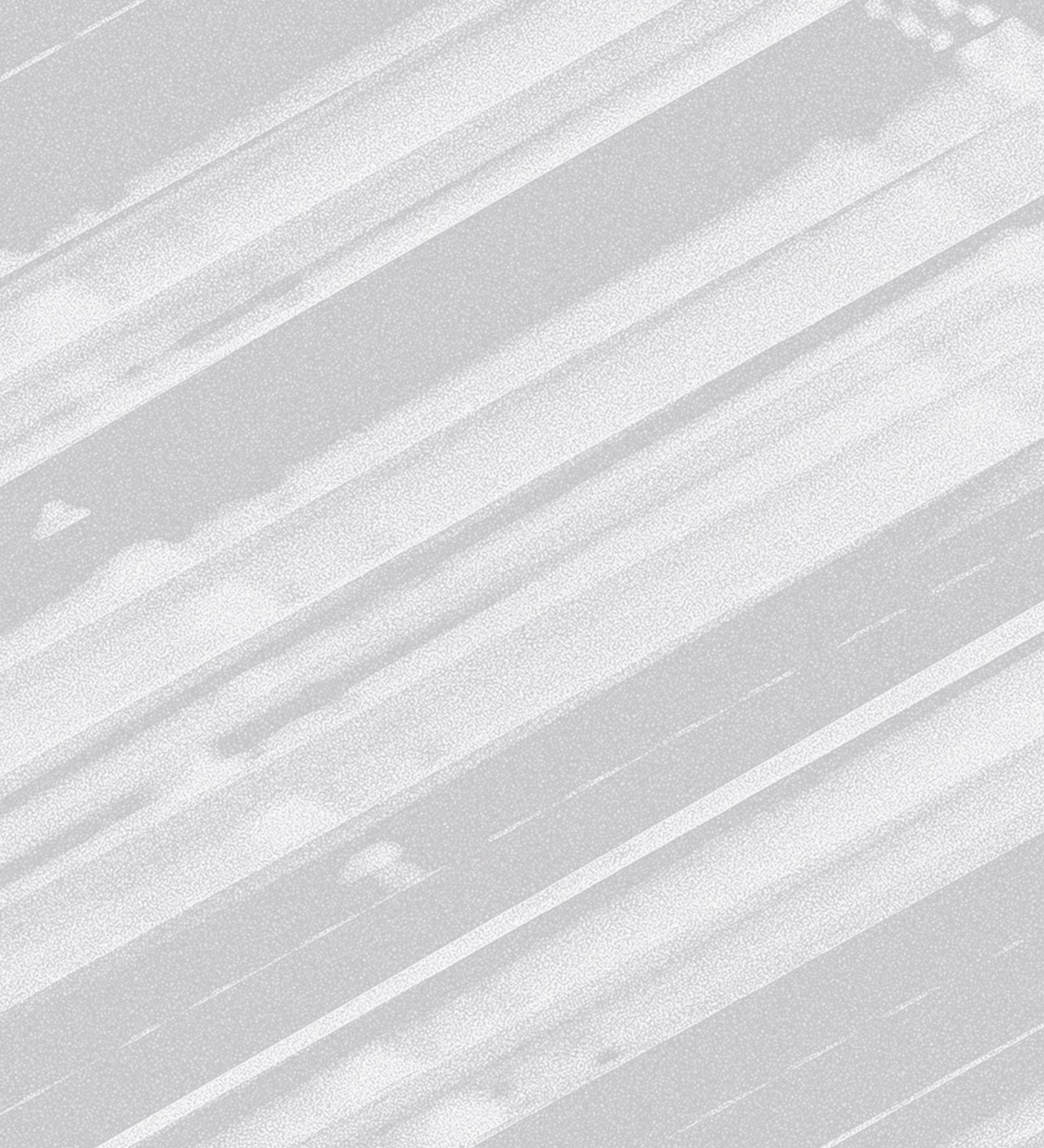
Lina Gautama is a South-East Asia expert, focusing particularly on Indonesia, Malaysia and Thailand. An Indonesian national, she has advised clients on political, commercial and integrity risks across the region.

As well as handling complex investigations in sectors such as mining, oil and gas, and the automotive industry, Lina has also delivered anti-bribery and anti-corruption assessments for foreign investors and overseen pre-transaction investigative due diligence projects across the region.

Prior to joining Argo Associates, Lina worked with Control Risks, Keppel and ConocoPhillips. She holds a bachelor's degree in Business from Singapore Management University. Lina is fluent in Bahasa Indonesia, Bahasa Melayu and Mandarin, and speaks some French, Spanish and Thai.



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